

## WIPRO LIMITED

### Some improvement, but still risky

**Wipro continues its organisational revamp focused on improving its account mining process. Steps have been taken to simplify reporting structures, standardise back-end processing and external consultants have been asked to bring the best practices. We find confidence returning to management that the company will be able to match peers' growth going forward despite the uncertainty in the demand environment. However, we believe that the turnaround could take more time and that the execution risks are not correctly priced. The stock is trading at a P/E of 15.7x for FY13 (7% discount to Infosys) and, hence, is not inexpensive. We maintain our 3-UW rating.**

**Simplifying organisational structure:** Reporting lines have been restructured so that sales and delivery primarily report to vertical heads. Senior level hires are being made to improve processes in both sales and delivery.

**End-demand improvement in specific pockets:** Wipro has seen end-demand stability since the beginning of the calendar year with traction in BPO and IT Infrastructure. Oil & Gas, BFSI, Retail and Healthcare are the key focus areas and likely growth drivers.

**Acquisition-led strategy to continue:** According to management, Wipro's acquisitions through the decade have had 2.2ppts accretion on the revenue CAGR with an IRR of 22%. With 20% of the current FY revenues from acquisitions, the company is unlikely to relent on its strategy and could continue to focus on smaller acquisitions.

**Execution risk makes us cautious:** The strong focus on top-line growth could imply a reduced margin focus near term. Given volatile environment and the changing organisational structure, there remains risk to earnings growth, in our opinion. Valuations at a P/E of 15.7x also do not provide much support. We retain 3-UW with PT of Rs360.

#### WIPR.NS: Quarterly and Annual EPS (INR)

FY Mar	2011		2012			2013			Change y/y	
	Actual	Old	New	Cons	Old	New	Cons	2012	2013	
Q1	N/A	5.47A	5.47A	N/A	6.54E	6.54E	N/A	N/A	20%	
Q2	N/A	5.33A	5.33A	N/A	6.56E	6.56E	N/A	N/A	23%	
Q3	N/A	5.94A	5.94A	N/A	6.90E	6.90E	N/A	N/A	16%	
Q4	N/A	6.47E	6.47E	N/A	7.05E	7.05E	N/A	N/A	9%	
Year	N/A	23.21E	23.21E	N/A	27.06E	27.06E	N/A	N/A	17%	
P/E	N/A		18.3			15.7				

Source: Barclays Capital  
Consensus numbers are from Thomson Reuters

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PLEASE SEE ANALYST(S) CERTIFICATION(S) AND IMPORTANT DISCLOSURES BEGINNING ON PAGE 8.

Stock Rating	<b>3-UNDERWEIGHT</b> Unchanged
Sector View	<b>2-NEUTRAL</b> Unchanged
Price Target	<b>INR 360.00</b> Unchanged

Price (27-Feb-2012)	INR 424.25
Potential	-15%
Upside/Downside	
Tickers	WPRO IN / WIPR.NS

Market Cap (INR mn)	1075670
Shares Outstanding (mn)	2458.39
Free Float (%)	20.90
52 Wk Avg Daily Volume (mn)	0.1
Dividend Yield (%)	1.4
Return on Equity TTM (%)	21.71
Current BVPS (INR)	111.50

Source: FactSet Fundamentals

Price Performance	Exchange-BSE
52 Week range	INR 490.15-310.20



[Link to Barclays Capital Live for interactive charting](#)

#### Asia Ex-Japan Software & IT Services

##### Bhuvnesh Singh

+91 22 6719 6314

bhuvnesh.singh@barcap.com

BSIPL, Mumbai

Vaibhav Dhasmana

+91 22 6719 6043

vaibhav.dhasmana@barcap.com

BSIPL, Mumbai

## COMPANY SNAPSHOT

## Wipro

Asia ex-Japan Software &amp; IT Services

Income statement (INRmn)	2011A	2012E	2013E	2014E	CAGR
Revenue	310,542	377,472	434,183	493,822	16.7%
EBITDA	65,878	76,084	88,390	99,285	14.7%
EBIT	57,667	65,916	75,541	84,997	13.8%
Pre-tax income	62,385	70,359	83,937	96,840	15.8%
Net income	52,974	56,765	66,322	76,515	13.0%
EPS (INR)	21.74	23.21	27.06	31.22	12.8%
Diluted shares (mn)	2,436	2,445	2,451	2,451	0.2%

Stock Rating	3-UNDERWEIGHT
Sector View	2-NEUTRAL
Price (27-Feb-2012)	Rs 424
Price Target	Rs 360
Ticker	WPRO IN / WIPR.NS

## Investment case

**Why a 3-Underweight? Weak execution of the company should continue to weigh on growth. This would keep share prices depressed leading to a valuation at a 30% discount to Infosys and our target price of Rs360.**

Margin and return data (%)	Average				
EBITDA margin	21.2	20.2	20.4	20.1	20.5
EBIT margin	18.6	17.5	17.4	17.2	17.7
Pre-tax margin	20.1	18.6	19.3	19.6	19.4
Net margin	17.1	15.0	15.3	15.5	15.7
ROIC	23.5	21.5	23.0	26.8	23.7
ROA	15.1	13.7	13.6	13.6	14.0
ROE	24.3	21.6	20.8	19.6	21.6

Upside case **Rs 510**

A strong rebound in discretionary IT spending or a much better-than-expected improvement in operations could lead to both EPS (+10%) and multiples (to 16x) upgrades. This would lead to a target of Rs510.

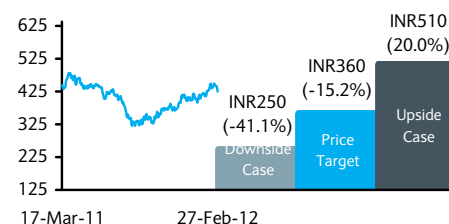
Balance sheet and cash flow (INRmn)	CAGR				
Fixed assets	55,094	59,950	59,101	56,812	1.0%
Cash and equivalents	112,132	117,079	202,851	266,151	33.4%
Total assets	371,443	454,915	519,639	601,912	17.5%
Current liabilities	67,575	98,728	108,914	124,101	22.5%
Long term liabilities	63,497	70,142	58,356	48,927	-8.3%
Total liabilities	131,763	169,661	168,061	173,819	9.7%
Net debt/(funds)	(59,330)	(58,148)	(155,706)	(228,435)	NA
Shareholders' equity	239,680	285,254	351,578	428,093	21.3%
Change in working capital	(5,357)	(21,345)	30,386	(6,075)	NA
Cash flow from operations	55,828	45,588	109,557	84,729	14.9%
Capital expenditure	(9,847)	(15,024)	(12,000)	(12,000)	NA
Free cash flow	45,981	30,564	97,557	72,729	16.5%

Downside case **Rs 250**

Significantly weaker macro scenario, or some further issues with restructuring could lead to both EPS downgrades (down 15%) and multiple correction (to 10x) leading to a share price of Rs250.

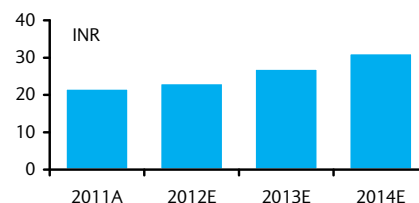
Valuation and leverage metrics	Average				
P/E (x)	19.5	18.3	15.7	13.6	16.8
EV/EBITDA (x)	14.8	12.9	10.0	8.2	11.5
FCF yield (%)	4.4	2.9	9.4	7.0	5.9
EV/sales (x)	3.1	2.6	2.0	1.6	2.4
Price/BV (x)	4.3	3.6	3.0	2.4	3.3
Dividend yield (%)	-	0.0	0.0	0.0	0.0
Total debt/capital (%)	18.1	17.1	11.8	8.1	13.8
Net debt/EBITDA (x)	(0.9)	(0.8)	(1.8)	(2.3)	1.4

## Upside/downside scenarios



Source: Thomson Reuters Datastream, Barclays Capital est.

## EPS projections



Source: Company data, Barclays Capital estimates

Note: FY end Mar

## Meeting with Wipro's CFO

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**We met Wipro's CFO, Suresh Senapathy, recently to get an update on the business.**

### **Key restructuring initiatives**

- Wipro is continuing its sales force restructuring with a third-party consulting firm engaged to suggest improvements.
- The company has started to focus on back-end standardisation, folding practices together to remove redundancies.
  - The entire RTB (Run the Business) related delivery has been brought under B.M. Bhanumurthy, who is the chief business operations officer for the company.
  - The CTB (Change the Business) related delivery will be headed by a new senior level hire (already onboard) to bring in efficiency for competitiveness.
- Sales force is being incentivised on not just the achievement of sales targets but also improving the DSOs.
- Focusing on improvement of account mining activities.
- Another senior level hire has been made to increase pursuing of new accounts (“hunting”).
- Wipro has been conscious about managing costs. In particular, subcontracting increased in 2Q-3Q FY12. The immediate focus is to reduce this.

### **Stabilisation in end demand**

Wipro has seen stabilisation in its end demand since the beginning of the calendar year. The investment banking segment has shown the first signs of a revival. Among the service offerings, Wipro is seeing improved traction with BPO and IT services clients.

Figure 1: Wipro – recent revenue growth by business segment, vertical and geography

	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	% q/q	% y/y
<b>By vertical</b>							
Technology, Media and Telecom	329	344	236	231	232	0.3%	-29.6%
Financial Services	367	374	376	399	411	3.0%	12.0%
Manufacturing	200	210	277	280	286	2.2%	42.8%
Healthcare and services	108	111	144	144	151	4.3%	40.0%
Retail & Transportation	207	218	211	216	224	3.6%	8.4%
Energy & Utilities	133	143	163	202	202	0.0%	51.6%
<b>By business segment</b>							
Infrastructure services	288	302	305	325	327	0.4%	13.6%
Testing services	148	148	90	97	99	2.2%	-32.8%
Package implementation	177	186	428	449	464	3.2%	161.3%
BPO	125	137	131	130	128	-1.3%	2.4%
Product Engg.	65	69	117	124	126	2.2%	96.0%
ADM	542	557	336	348	361	3.9%	-33.3%
<b>By geography</b>							
US	728	755	746	761	790	3.8%	8.5%
Europe	380	392	403	424	424	0.1%	11.6%
Japan	20	21	15	19	20	2.2%	-2.9%
India & Middle East	120	127	127	137	137	0.0%	14.5%
Other Emerging Markets	95	105	117	131	134	2.2%	40.4%
<b>Total</b>	<b>1,344</b>	<b>1,400</b>	<b>1,408</b>	<b>1,473</b>	<b>1,505</b>	<b>2.2%</b>	<b>12.0%</b>

Source: Company data, Barclays Capital

### Acquisition-led growth strategy likely to continue

Wipro has been amongst the most active in the inorganic growth strategy within the peer group. The company has made acquisitions valued at US\$1.2bn through the decade, which have yielded an overall IRR of 22%. These acquisitions have increased the decade-long CAGR of the company by 2.2ppts and are contributing to 20% of the current year revenues.

Wipro is likely to continue its acquisition-led strategy with a focus on smaller-size targets within the focus verticals of the company.

Figure 2: Wipro – history of acquisitions throughout the past decade

Effective Date	Target Business	Country	% stake acquired	Deal size (mn)	Domain
Jun-11	RKM Equipamentos Hidraulicos	Brazil		Undisclosed	Diversified manufacturing
Jun-11	SAIC Inc	US	100	USD 150.0	Consulting services
Dec-09	Yardley Business	UK	100	USD 45.5	Cosmetics & Toiletries
Mar-09	3D Networks	India		USD 30.0	Computer Services
Jan-09	Citi Technology Services	India	100	USD 127.0	Enterprise Software / Services
Jul-08	Gallagher Financial Systems	US	100	Undisclosed	Commercial Serv-Finance
Jun-08	WMNetServ	UK	50	Undisclosed	Telecom Services
Oct-07	Oki Electric Industry Co	Singapore	100	Undisclosed	Telecommunication Equipment
Sep-07	Infocrossing Inc	US	100	USD 547.9	Data Processing / Management
Jul-07	Unza Holdings Pte	Singapore	100	INR 10,102.0	Cosmetics & Toiletries
Mar-07	Enabler	Portugal	100	EUR 41.0	Consulting services
Jan-07	Hydrauto Group AB	Sweden	100	USD 31.0	Auto-Med & Heavy Duty Trucks
Nov-06	3D Network and Planet PSG	Singapore	100	SGD 23.0	Telecom Services
Jul-06	Quantech Global Services LLC	US	100	Undisclosed	Engineering / R&D Services
Jun-06	Saraware Oy	Finland	100	EUR 25.0	Application Software
May-06	North-West Switchgear Ltd	India	100	INR 1,022.0	Electric products-Misc
Apr-06	cMango Inc	US	100	USD 20.0	Consulting services
Dec-05	Mpower Inc	US	100	USD 28.0	Finance-other services
Dec-05	NewLogic Technologies	Austria	100	EUR 47.0	Electronics Compo-Semicon
May-03	Wipro NerveWire Inc	US	100	USD 18.7	Consulting services
Apr-03	Glucose Drink Band	India	100	Undisclosed	Beverages-Non-alcoholic
Jan-03	Telefonnaktiebolaget LM Ericsson	India	100	Undisclosed	Application Software
Jan-03	Spectramind eServices	India	8	Undisclosed	Telecom Services
Nov-02	CGI Technologies and Solutions	US	100	USD 26.0	Data Processing / Management
Sep-02	Spectramind eServices	India	2	USD 3.50	Telecom Services
Aug-02	Spectramind eServices	India	66	INR 4,069.00	Telecom Services
Jul-02	GE Medical Systems IT	India	100	USD 5.73	Application Software
Oct-01	Spectramind eServices	India	17	INR 480.00	Telecom Services
Dec-00	Wipro Net Ltd	US	47	EUR 25.62	
Feb-00	Wipro Acer Ltd	India	100	Undisclosed	

Source: Company data, Bloomberg, Barclays Capital

### Revenue growth to track peers, margin upsides limited

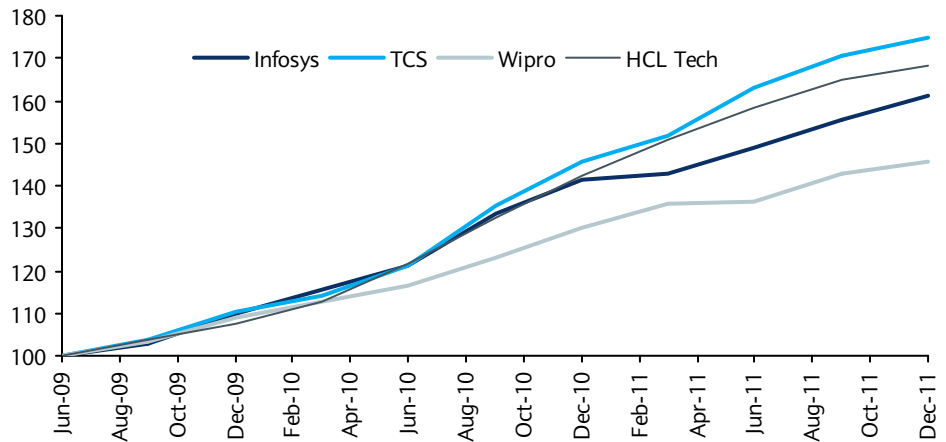
Wipro has undertaken a significant restructuring post the setup of a new management structure over a year ago. It has focused on changing multiple domains within the organisation in one go, right from sales to back-end. This has brought back revenue growth to be in line with peers in the Dec-11 quarter with guidance for Mar-12 slightly ahead.

## Key risks

We see **three key risks** on stock in view of the recent run-up going forward:

- Despite Dec-11 growth and Mar-12 guidance being a positive, Wipro still needs to show sustained growth in line with peers to warrant a permanent rerating, in our view.

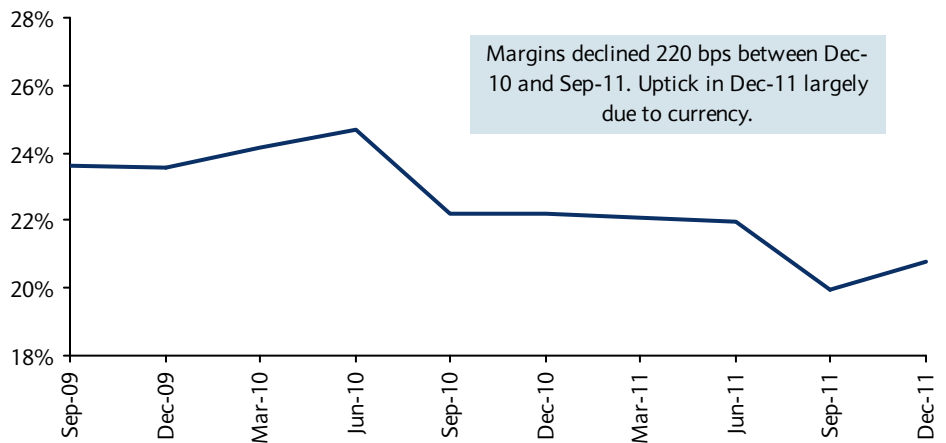
**Figure 3: Revenues of the Top-4 Indian IT vendors rebased to 100 as of Jun-09**



Source: Company data, Barclays Capital

- Investments in sales and marketing as well as the back-end revamp are likely to inhibit any margin improvement in the next two years with a possibility of quarterly volatility as margin levers are reduced.

**Figure 4: Wipro – quarterly EBIT margins**



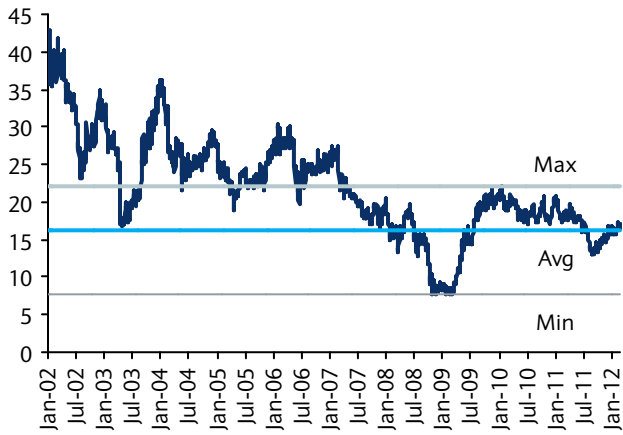
Source: Company data, Barclays Capital

- Wipro's decade-long revenue growth would have lagged peers even more had it not been for the 2.2ppt accretion from the acquisitions. A combination of the ongoing internal restructuring with the acquisition strategy carries a significant execution risk in our view.

## Valuations

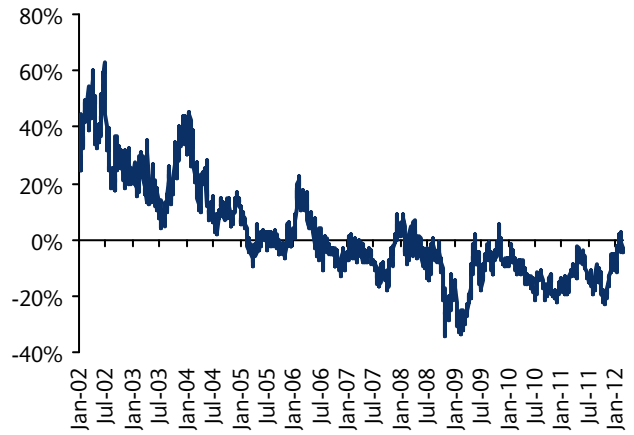
The stock has tracked the strong sector performance recently. It is trading in line with its historical trading averages and Infosys' 12-month forward P/E.

Figure 5: Wipro – 12-month forward P/E (x)



Source: Datastream, Barclays Capital

Figure 6: Wipro – 12-month forward P/E (x) relative to Infosys



Source: Datastream, Barclays Capital

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Wipro Limited (WIPR.NS, 27-Feb-2012, INR 424.25), 3-Underweight/2-Neutral

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In addition to the stock rating, we provide sector views which rate the outlook for the sector coverage universe as 1-Positive, 2-Neutral or 3-Negative (see definitions below). A rating system using terms such as buy, hold and sell is not the equivalent of our rating system. Investors should carefully read the entire research report including the definitions of all ratings and not infer its contents from ratings alone.

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**2-Neutral** - sector coverage universe fundamentals/valuations are steady, neither improving nor deteriorating.

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Asia Ex-Japan Software & IT Services

HCL Technologies (HCLT.NS)

Infosys Ltd. (INFY.NS)

Tata Consultancy Services (TCS.NS)

Wipro Limited (WIPR.NS)

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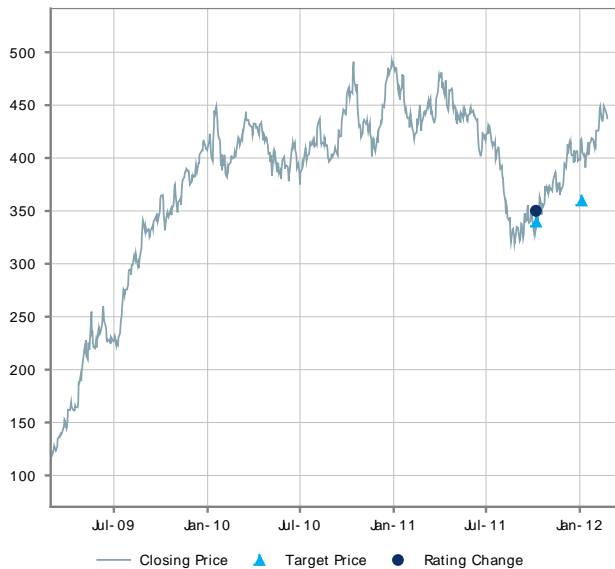
**Wipro Limited (WPRO IN / WIPR.NS)**  
**INR 424.25 (27-Feb-2012)**

Stock Rating  
**3-UNDERWEIGHT**

Sector View  
**2-NEUTRAL**

Rating and Price Target Chart - INR (as of 27-Feb-2012)

Currency=INR



Date	Closing Price	Rating	Price Target
04-Jan-2012	417.90		360.00
07-Oct-2011	333.80	3-Underweight	340.00

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**Valuation Methodology:** Our 12-month target price of INR360 for Wipro is based on a P/E of 12x, which we apply to the average of our EPS estimates for FY2013 and FY2014. For Wipro, our target multiple is based on a 30% discount to our target multiple of 17.5x for Infosys, which is at the low end of Wipro's historical discount because we perceive a higher risk to Wipro's earnings growth going forward.

**Risks which May Impede the Achievement of the Price Target:** The key risks to the upside that could keep our price target from being achieved are a stronger-than-forecast rebound in the macroeconomic situation and better-than-expected execution by the new management team. We note that while the company has always had the industry expertise, it has historically had lapses in execution that have hindered growth. Turnaround by the new management could drive upsides to our forecasts. Key downside risk would come from macroeconomic factors that could further impede the company's already slow growth profile relative to its peers.

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